1976

Bank of Ephraim v. Halbert Davis et al : Brief of Respondent

Utah Supreme Court

IN THE SUPREME COURT OF THE STATE OF UTAH

BANK OF EPHRAIM, a Utah corporation, Plaintiff-Appellant vs. HALBERT DAVIS, STEVIE KAY STEINMANN, BABYLON CORPORATION, PRUDENTIAL FEDERAL SAVINGS, FIRST STATE BANK, THE UTAH TAX COMMISSION, and UNITED STATES OF AMERICA, Defendants-Respondents.	)	Case No. 14514

BRIEF OF RESPONDENT
BABYLON CORPORATION

APPEAL FROM THE JUDGMENT OF THE DISTRICT COURT
IN AND FOR SANPETE COUNTY, UTAH
THE HONORABLE DON V. TIBBS, JUDGE, PRESIDING.

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STATEMENT OF THE NATURE OF THE CASE

The appellant Bank of Ephraim appeals from a decision of the Sixth Judicial District Court as to the priorities of certain judgment creditors on a Judgment and Decree of Foreclosure.

DISPOSITION IN LOWER COURT

The District Court awarded judgment on a Decree of Foreclosure to the judgment creditors, Bank of Ephraim, Babylon Corporation, Prudential Federal Savings & Loan Association and the Utah State Tax Commission, as per the complaints of each creditor. The rights of the defendant Steinmann were previously assigned to defendant Babylon Corporation. The defendants, First State Bank and United

States of America, were previously dismissed as parties defendant to the action.

In its Judgment and Decree of Foreclosure, the District Court, in addition to awarding judgments to the judgment creditors, assigned priorities to the judgments of each creditor, as set forth in the appellant's Statement of Facts.

RELIEF SOUGHT ON APPEAL

Respondent seeks to sustain the entry of judgment and priorities as set forth in the court below.

STATEMENT OF FACTS

For purposes of the issues raised in this appeal, respondent substantially accepts the Statement of Facts of appellant, with several clarifications and additions as follows:

1. Appellee Babylon Corporation has interest only in the cafe property. Babylon Corporation obtained this interest by assignment from Steven Kaye Steinmann.

2. The mortgage that Halbert Davis gave to Steinmann was given the same day that the Bank of Ephraim note was given - August 7, 1970. (See defendant's Exhibit #5).

3. The Steinmann mortgage was recorded after the Bank of Ephraim mortgage, but on the same day - August 10, 1970. (See defendant's Exhibit #3). At the time of the recordation of the Steinmann mortgage, the Bank of Ephraim had advanced only $2400.00 on the Bank of Ephraim note. Any monies advanced by the Bank of Ephraim on the cafe property over and above $24[illegible]

were advanced after the recordation of the Steinmann mortgage, and were purely optional. (Appellant's Brief, p. 9).

4. The Steinmann mortgage was recorded at the request of Tibbs & Tervort, who then were counsel for the appellant, Bank of Ephraim. (See defendant's Exhibit #3). The fact that the deed was prepared by the escrow department of the Bank of Ephraim, and was recorded at the request of counsel for the appellant is important in establishing that as of August 10, 1970, the appellant had actual notice of the Steinmann mortgage.

5. As stated by the appellant, "the mortgage to Steven Kaye Steinmann expressly sets forth the fact that it was secondary to the mortgage of the Bank of Ephraim." What the appellant failed to mention is that the Steinmann mortgage expressly sets forth that it be second in lien priority to the Bank of Ephraim mortgage in the amount of $2400.00. (Defendant's Exhibit #3).

ARGUMENT

POINT I

APPELLANT BANK OF EPHRAIM HAS NO BASIS IN LAW OR IN FACT FOR ITS APPEAL AGAINST THE APPELLEE, BABYLON CORPORATION.

Throughout its arguments, appellant addresses itself to appellee Prudential Federal Savings, and only in the closing one-half page is Babylon Corporation even mentioned. Appellant would have the Court believe that the facts of the Babylon mortgage are in relevant parts similar to the facts of the Prudential mortgage. Such is not the case. The Babylon mortgage differs from the Prudential mortgage in two very important

respects. First, the Bank of Ephraim had actual notice of the Babylon mortgage, and thus was put on notice of a lien superior to its future optional advances. Second, all advances made by the Bank of Ephraim on the cafe property were made after the giving of the Steinmann mortgage. As will be pointed out below, these two fact differences render inapplicable all of the appellant's arguments as appellant would have the Court apply them to Babylon Corporation. Indeed, the cases cited by the appellant support conclusively the position of the appellee, Babylon Corporation.

POINT II

BECAUSE THE BANK OF EPHRAIM HAD ACTUAL NOTICE OF THE BABYLON MORTGAGE, AND ALL OF THE APPELLANT'S ADVANCES WERE MADE AFTER THE RECORDATION OF THE BABYLON MORTGAGE, THE BABYLON LIEN HAS PRIORITY OVER ANY MONIES OPTIONALLY ADVANCED BY THE BANK OF EPHRAIM.

The appellant has admitted from the beginning that the advances made by the Bank of Ephraim were optional and not obligatory under the mortgage. (Appellant's Brief, p. 9). Authority almost universally advises that such advances, when given after notice of subsequent interests, do not have priority over such subsequent interests. The universal rule is quoted quite succinctly in Leche v. Ponca City Production Credit Association, 478 P.2d 347, 350 (Okla. 1970):

> "The applicable rule of law is stated in 36 Am. Jur., Mortgages, §234: 'The greater array of authority, however, is found on the side of the doctrine that advances made after notice of subsequent interests

> do not have priority over such interests. This rule has been applied to subsequent liens and encumbrances as well as to subsequent grants of the property. The mere specification in the senior mortgage that the further advances are not to exceed a fixed sum does not vary the rule. The rule is especially applicable where the advancements are optional with the mortgagee...'
>
> In 59 C.J.S., Mortgages, §230, at 299, the rule is stated: 'In accordance with the general rule, after notice of the attaching of a junior lien, the senior mortgagee ordinarily will not be protected in making further advances under his mortgage given to secure such advances, at least where he was under no binding engagement to make such advances.'"

The above cited case is not a materials men case, yet it does come down strongly to support Babylon's position.

Other courts almost universally agree. In Kimmel v. Batty, 168 Colo. 431, 451 P.2d 751, 753 (1969), the Supreme Court of Colorado approves of the rule that "...if it is optional with the mortgagee to make or refuse the advances, he will be protected by the security of his mortgage only as to the advances made before the attaching of the junior lien or encumbrance." (emphasis added).

The Supreme Court of Washington, in National Bank of Washington v. Equity Investors, 81 Wash.2d 886, 506 P.2d 20, 29 (1973), also strongly agrees:

> "Thus, we are adhering to what we perceive to be the weight of authority... Optional advances under a construction loan agreement attach when the advances

> are actually made. Any liens attaching prior to an optional advance would thus be superior to it, and attaching afterwards, junior to it."

The Idaho Supreme Court has also come down on point:

> "A senior mortgage for future advances will maintain seniority for advances made after actual notice of a junior lien if, but only if, there was a contractual obligation to make such advances existing prior to the notice of the junior lien." Biersdorff v. Brumfield, 93 Ida. 569, 468 P.2d 301, 302 (1970).

The appellant cites Savings & Loan Society v. Burnett, 106 Cal. 514, 39 P. 922, 926 (1895) as being controlling. In that case, quoting from Tapia v. Demartini, 77 Cal. 387, 641 (1888), the California Court states:

> "But the lien of the mortgage cannot be enforced against subsequent encumbrances, of which the mortgagee has actual notice for advances or endorsements made or given after such notice."

A review of other cases cited by the appellant indicates that Iowa, Indiana and Alabama, as well as virtually all other jurisdictions, support the position that optional advances by a prior lienholder, after that prior lienholder has been given notice of subsequent interests, do not have priority over such subsequent interests. (See Everist v. Carter, 202 Iowa 4[illegible] 210 NW 559 (1926); Corn Belt Trust & Savings Bank of Bell[illegible] Plaine v. May, 197 Iowa 54, 196 NW 735 (1924); Schmidt v. Zahrndt, 148 Ind. 447, 47 NE 335, 337 (1897); Farmers Un[illegible] Warehouse Co. v. Barnett Bros., 273 Ala. 435, 137 So. 1[illegible] (1931); Elmendorf-Anthony Co. v. Dunn, 10 Wa.2d 29, 11[illegible] 253, 255 (1941)).

In reaching this rule of law, the courts have followed good sound reasoning and policy. If the courts allowed a first mortgage holder to make optional advances with priority ad infinitum, even after receiving notice of a second mortgageholder's interest, it would spell the death of the second mortgage. In the instant case, it should be obvious to the Court that the Babylon-Steinmann mortgage would not have been accepted for security if Steinmann had known that the Bank of Ephraim would attempt to take priority on all future optional advances, totally contrary to the law. The appellant Bank of Ephraim indicates that any future lienholders have the responsibility of ascertaining the true amount of indebtedness outstanding at the time that the second mortgage is put into effect - even when the amount cannot be determined from the face of the mortgage (Appellant's Brief, p. 11). This is true, and Steinmann took all possible steps to protect herself, by indicating that her mortgage was second to that of the Bank of Ephraim in the amount of $2400.00. (The exact amount already advanced). Bank of Ephraim, being the escrow agent in the Steinmann transaction, had actual notice of the above restriction. Therefore, in law and in policy, Bank of Ephraim should not receive priority over Steinmann-Babylon for any monies advanced after notice and recordation of the Steinmann-Babylon mortgage.

The Court will note that the above panoply of law indicates that the Babylon Corporation should receive priority for all amounts over the $2400.00 already advanced at the time of the

Steinmann-Babylon mortgage, rather than amounts over $3000., as decided in the court below. Although Babylon Corporation did raise this point in the court below, it has not proferre this point as a grounds for appeal and, therefore, does not ask for reversal of the lower court's judgment.

POINT III

THE INCLUSION IN THE BANK OF EPHRAIM MORTGAGE OF THE TYPEWRITTEN PHRASE "THE PRINCIPAL AMOUNT NOT TO EXCEED $3000.00" LIMITS THE BANK'S PRIORITY AND RECOVERY ON THE MORTGAGE TO $3000.00.

Although the multiplicity of authority under Point II should suffice to obtain the results for which the appellee, Babylon Corporation, asks, there is also solid authority whi indicates that the $3000.00 limitation typed onto the Bank o Ephraim mortgage also may be conclusive.

Appellant contends that the printed word in paragraph 1 of the Bank of Ephraim mortgage, wherein it states "and for all of which this mortgage shall stand as a continuing secur until paid" should supercede the large typed statement that "this mortgage covers all additional advances on this loan, the total principal amount not to exceed $3000.00." The typed statement is obviously a limitation on the mortgage security, and is irreconcilable with any statements which w allow unlimited security.

The Bank of Ephraim mortgage was prepared by the appel lant, and thus should be construed most strongly against i

> "...In case of uncertainty as to the meaning of a contract, it should be construed most strictly against its framer..." (Seal v. Tayco, Inc., 16 U.2d 323, 380 P.2d 503 (1965).

Additionally,

> "Where there is a printed form of a contract, and other words are inserted, in writing or otherwise, it is to be assumed that they take precedence over the printed matter." (Holland v. Brown, 15 U.2d 422, 394 P.2d 77, 78 (1964)).

In the same light, Steven Kaye Steinmann was justified, when reviewing the Bank of Ephraim mortgage, to believe that the written (typed) word would take precedence over any ambiguous printed statements. A mortgage cannot be both "for any other indebtedness at any time existing from the mortgagor to the mortgagee," and limited in principal amount "not to exceed $3000.00," unless the total debt outstanding is always $3000.00 or less. Because of the typed clause in the instant case, once the principal amount reaches $3000.00, any additional advances would not be secured under the mortgage.

A fine Utah case in point is General Mills, Inc. v. Cragun, 103 Utah 239, 134 P.2d 1089 (1943), in which a unanimous decision was rendered, and has stood the test of time of over 33 years. In the General Mills case, there was a chattel mortgage securing the mortgagors' obligation to pay for turkey feed, drawn by the mortgagee. That mortgage contained two clauses which are amazingly similar to the clauses in question in the instant case. First, in the body of the printed mortgage, it is stated that the mortgage was security for "all other sums now or hereafter due or owing from the mortgagors to the mortgagee." Closely following was the limit "provided, however, that the maximum amount, the payment of which is to

be secured hereby, is $3750.00." The court decided that both clauses could not be operative; that there was an irreconcilable ambiguity, and therefore rules of construction and interpretation were to be followed. Quoting from the text of the opinion at page 1093:

> "It is so elementary that an ambiguity in a written instrument is construed more strongly against the party who drew the instrument that citation of authorities should be unnecessary. This is especially so where the one drafting the instrument has the advantage of a lender of money." (emphasis added).

After a thorough consideration of law and policy, the court finally stated, at 1094, that:

> "We are constrained to hold from a consideration of the language of the contract in its entirety, the contract res and the relation of the parties to each other, that the parties intended by their agreement to enter into a chattel mortgage to secure the sum of not to exceed $3750.00 by a lien..."

The similarities in the two cases are striking. Both cases involved mortgages. In both cases the mortgagee prepared the mortgage papers. Both cases have an 'unlimited' security clause as well as a 'limiting' clause. The law in Utah is clear, that there is a limiting clause in a mortgage, "the mortgage involved is in fact for an liquidated amount with a maximum..." (General Mills, supra, at 1093).

As applied to the case at bar, the General Mills case clearly indicates that any priorities that the appellant Bank of Ephraim could have on the secured cafe property stop at $3000.00, as indicated on the fact of the mortgage. To grant more would be going against at least 33 years of clear-cut

law, as well as policy which dictates that ambiguities in written instruments (and in particular, recorded instruments designed to give notice) should be construed most strongly against the preparer of the instrument.

CONCLUSION

The appellant argues almost exclusively against Prudential Federal Savings, and never comes on point against the appellee Babylon Corporation. As extensively cited in Point II, the universal rule is that advances given after notice of subsequent interests do not have priority over such subsequent interest. Finally, the $3000.00 express limit as typed onto the face of the mortgage limits any priorities of the Bank of Ephraim under the mortgage of $3000.00. Both extensive law and common sense policy dictate that the judgment of the lower court should be affirmed in its entirety as it applies to the appellee Babylon Corporation.

Respectfully submitted,

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CERTIFICATE OF MAILING

This is to certify that I mailed two (2) copies of the

foregoing Brief to Louis G. Tervort, Attorney for Plaintiff-Appellant, 50 North Main, Manti, Utah 84642, and to Wayne C. Petty, Moyle & Draper, Attorneys for Prudential Federal Savings & Loan, No. 15 East First South, Salt Lake City, Utah 84111, and to Bruce M. Hall, Assistant Attorney General, State Capitol Building, Salt Lake City, Utah 84114, and to Udell R. Jensen, Attorney for Halbert Davis, 125 South Main, Nephi, Utah 84648, this 6th day of August, 1976.

S. Rex Lewis